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U.S. GENERAL SERVICES ADMINISTRATION

BEFORE THE

**SUBCOMMITTEE ON ECONOMIC DEVELOPMENT,
PUBLIC BUILDINGS, AND EMERGENCY MANAGEMENT**

**COMMITTEE ON
TRANSPORTATION AND INFRASTRUCTURE**

U.S. HOUSE OF REPRESENTATIVES

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Good morning, Madam Chair, Ranking Member Graves, and Members of the Subcommittee. My name is David L. Winstead and I am the Commissioner of Public Buildings at the U.S. General Services Administration (GSA). Thank you for inviting me here today to discuss the impact of the tightening of the credit markets on GSA's capital program.

New Construction and Modernizations

Because they are funded through appropriations, our new construction, modernization, and repair and alteration programs are not directly affected by any decreases in the availability of credit generally. GSA pays contractors and subcontractors for these projects periodically for work completed; they typically do not need to obtain third-party financing to complete these segments.

Leasing

Nationally, GSA is noticing some impact of the credit crunch on its leasing program. We asked each of GSA's regional offices whether GSA offerors were experiencing difficulty obtaining financing for GSA lease projects. Generally, the responses from the GSA regions suggest that successful GSA offerors are obtaining financing on more costly terms in comparison to previous years. More costly leasing terms, of course, generally result in higher rental rates for the Government. However, financing for Government deals (where leases are backed by the full faith and credit of the United States) has always been lower than that for more risky ventures. Therefore, when credit becomes more expensive or difficult to obtain, lessors of Government-leased buildings have typically obtained financing more easily and on less costly terms than other borrowers.

In a few instances, successful GSA offerors have been unable to obtain lease project financing and, as a result, have not been able to proceed with lease construction projects. Offerors have attributed this problem to the tighter credit market. For example, in 2005, GSA initiated a lease construction project for the FBI for up to

266,200 rentable square feet of space with 271 parking spaces in Detroit, Michigan. In May 2006, GSA finalized negotiations for a no-cost assignable option for a 10.2 acre site at 1200 6th Street in downtown Detroit, then used a two-phase, best-value source selection process to select a development team. We awarded the lease to a developer in February 2007. In October 2007, the developer indicated that, as a result of the tight credit market and the post-award addition of work to the project by the City of Detroit, it could not secure financing for the project at a rate that would support its expected returns and asked to withdraw. GSA and the developer completed a no-cost settlement agreement and GSA rescinded the contract in February 2008. While such an occurrence is not widespread for GSA, these projects are not going unnoticed.

Here testifying with us today is Jones Lang LaSalle, one of our national brokers. They will be able to tell you about the state of the real estate investment market generally.

As you may know, GSA uses credit tenant leases (CTL) in some of its larger lease transactions in order to gain better lease rates through the most effective financing available. The CTL has been used with varying degrees of success in several GSA regions. Following a U.S. Government Accountability Office report encouraging GSA to adopt a more businesslike leasing approach, GSA modified its General Clauses in the CTL to enable better lessor financing for large transactions. Using the CTL, successful offerors may be able to obtain higher loan amounts, at lower interest rates. Under the CTL, once the leased space is delivered according to the lease requirements, the Government compromises on some of its termination and set off rights against the debt-servicing portion of the rental payments in order to allow an uninterrupted rental payment stream to service the lessor's debt. The Government retains its rights to enforce the lessor's service obligations. In order to ensure that we are obtaining the value of these lease modifications, we encourage our regions to request pricing on both our standard lease and our CTL so that we can see the savings.

Energy Savings Performance Contracts

Increasingly, we are relying on Energy Savings Performance Contracts (ESPC's) to accomplish energy saving capital improvements. Through an ESPC, an Energy Service Company (ESCO) conducts a comprehensive energy audit, identifies improvements that will save energy at the facility, and arranges financing to pay for them. The ESCO guarantees that the improvements will generate savings sufficient to pay for the project over the term of the contract. We estimate that our potential for ESPC and Utility Energy Services Contract use in FY2009 is approximately \$20 to 24 million. However, small and medium-sized ESCO's, who rely on bank or investor financing to fund ESPC's and do not have extensive track records, may find it increasingly difficult to obtain financing in this environment. ESPC financing is not traditional in that it is not asset-based; rather, it is backed by guaranteed energy savings resulting from the improvements. As a result, GSA and federal agencies generally may have to rely on larger ESCO's to perform ESPC contracts. This may affect other federal agencies more than GSA, since GSA's buildings tend to be large and therefore we tend to contract with larger ESCO's already.

Retail Leasing

Retail leasing amenities are an important consideration on several of our federal campuses - in particular, the Ronald Reagan Building & International Trade Center and the 8,000 square feet of restaurant and retail space adjacent to the new Bureau of Alcohol, Tobacco, Firearms and Explosives (ATF) headquarters building. Banks have begun tightening standards for loans to small businesses. We understand that this is making it harder to gain funding for anything from buying equipment to hiring new workers. So far, however, this more restrictive credit environment has had no discernable impact on GSA's retail leasing activities.

The Ronald Reagan Building & International Trade Center currently has full occupancy of all retail space. Three of the four retail tenants in the ATF headquarters building have

signed sub-leases and negotiations are currently being conducted with the fourth retail space. One establishment has already opened for business. The remaining businesses are slightly behind schedule because they must wait for Washington Gas to provide service to the facility; however they are on schedule to open by the end of August.

Conclusion

The tightening of the credit markets potentially affects GSA in three areas: leasing, energy savings performance contracting, and retail leasing. So far, none of these areas has been significantly affected. Credit is available to our lessors at relatively favorable rates with the Federal government as a major tenant. Federal agencies generally may experience an increased reliance on larger ESCOs for ESPC contracts because the financing for these is unconventional, backed solely by a stream of expected energy savings rather than an assets. Although some of the small businesses to which we lease our retail areas may experience difficulty due to a tightening of credit, we have not experienced a high level of vacancies so far.

Madam Chair, Ranking Member Graves, this concludes my prepared statement. I will be pleased to answer any questions that you or any other Members of the Subcommittee may have on the impact of the credit crunch on our capital program, or on any other aspects of the Public Buildings Service.